

Recent Developments in Valid-When-Made and True Lender Litigation

By Ashley Simonsen, Andrew Soukup, David A. Stein, Matthew Q. Verdin, and Stefan Caris Love*

INTRODUCTION

National banks and federal savings associations have the power under section 85 of the National Bank Act (“NBA”)¹ and section 4(g) of the Home Owners’ Loan Act (“HOLA”),² respectively, to make loans at the rate of interest allowed by the laws of their home states, without regard to other state law interest rate limitations, such as usury laws. State-chartered banks that offer deposits insured by the Federal Deposit Insurance Corporation (“FDIC”) have the same power under section 27 of the Federal Deposit Insurance Act (“FDIA”).³ Claims asserted against banks under the usury laws of other states (besides their home states) are preempted under these statutes. Moreover, under the “valid-when-made” doctrine, state laws that would be preempted in a lawsuit against a bank are also preempted in a suit against the bank’s assignee.⁴ By contrast, the interest rates on loans made by nonbanks generally must comply with the law of the borrower’s home state, regardless of where the nonbank is located.⁵

Because of this divergence, borrowers and state regulators sometimes argue that a loan made by a bank nevertheless violates state lending and usury laws, and preemption should not apply, due to the involvement of a nonbank. These challenges commonly take one of two forms. The first posits that even

* Ashley M. Simonsen is a partner in the Los Angeles office of Covington & Burling LLP who specializes in financial services litigation. Andrew Soukup is a partner in the Washington, D.C. office of Covington & Burling LLP who specializes in financial services litigation. David A. Stein is of counsel in the Washington, D.C. office of Covington & Burling LLP who specializes in providing regulatory advice on credit reporting, privacy, consumer financial services, and fintech. Matthew Q. Verdin is an associate in the San Francisco office of Covington & Burling LLP. Stefan Caris Love is a former associate at Covington & Burling LLP.

1. See 12 U.S.C. § 85 (2018).

2. Home Owners’ Loan Act § 4(g), 12 U.S.C. § 1463(g) (2018).

3. Federal Deposit Insurance Act § 27(a), 12 U.S.C. § 1831d(a) (2018).

4. See *Nichols v. Fearson*, 32 U.S. 103, 105 (1833) (calling it a “cardinal rule” that “a contract which in its inception is unaffected by usury can never be invalidated by any subsequent usurious transaction”); *Gaither v. Farmers’ & Mechanics’ Bank of Georgetown*, 26 U.S. 37, 43 (1828) (“[I]f the note [is] free from usury, in its origin, no subsequent usurious transactions respecting it can affect it with the taint of usury.”).

5. See, e.g., *Dopp v. Yari*, 927 F. Supp. 814, 819 (D.N.J. 1996) (determining New Jersey’s criminal usury law would apply to a transaction between a California lender and New Jersey borrower).

though the loan may have been valid when made by the bank, the subsequent sale, transfer, or assignment of the loan to a third party means that the loan no longer enjoys federal preemption because the nonbank could not have made the loan on the same terms. This is sometimes called a *Madden* argument, after the Second Circuit's controversial decision in *Madden v. Midland Funding, LLC*,⁶ which declined to recognize the valid-when-made doctrine in the context of a national bank's sale of charged-off credit card debt to a third-party debt collector.⁷

The second argument posits that preemption should not apply if, after applying a fact-intensive multi-factor test, it is determined that the bank is not the "true lender" on the loan—in other words, the loan's terms violated state law when the loan was first made. Litigants advancing "true lender" theories have sought to attack bank partnership models in which nonbank third parties provide underwriting and other services to state or federally chartered banks and then purchase loans made by the banks shortly after origination.

The need for regulatory clarity over this past year took on heightened importance, as courts continued to reach inconsistent decisions on the application of the valid-when-made and true lender doctrines. At the same time, federal regulators responded by issuing new regulations designed to remove uncertainty in the marketplace and participating in litigation as amici with greater frequency.

VALID-WHEN-MADE DEVELOPMENTS

NEW FEDERAL REGULATIONS

The most notable development on the valid-when-made front was the issuance of new federal rules that sought to resolve the legal uncertainty created by *Madden*. In June and July 2020, the Office of the Comptroller of the Currency ("OCC") and the Federal Deposit Insurance Corporation ("FDIC"), respectively, finalized rules providing long-awaited regulatory affirmation that a bank loan's rate of interest retains its non-usurious character when the loan is acquired by a third party.⁸ The final OCC rule provides that "[i]nterest on a loan that is permissible under [section 85 of the NBA and section 4(g) of the HOLA] shall not be affected by the sale, assignment, or other transfer of the loan."⁹ Similarly, the final FDIC rule provides that "[i]nterest on a loan that is permissible under section 27 of the [FDIA] shall not be affected by a change in State law . . . or the sale, assignment, or other transfer of the loan, in whole or in part."¹⁰ The FDIC

6. 786 F.3d 246 (2d Cir. 2015), *cert. denied*, 136 S. Ct. 2505 (2016).

7. *See id.* at 253.

8. Permissible Interest on Loans that Are Sold, Assigned, or Otherwise Transferred, 85 Fed. Reg. 33530, 33536 (June 2, 2020) (to be codified at 12 C.F.R. pts. 7 & 160) [hereinafter OCC Final *Madden-Fix* Rule] (effective Aug. 3, 2020); Federal Interest Rate Authority, 85 Fed. Reg. 44146, 44158 (July 22, 2020) (to be codified at 12 C.F.R. pt. 331) [hereinafter FDIC Final *Madden-Fix* Rule] (effective Aug. 21, 2020).

9. OCC Final *Madden-Fix* Rule, *supra* note 8, at 33536 (to be codified at 12 C.F.R. §§ 7.4001(e), 160.110(d)).

10. FDIC Final *Madden-Fix* Rule, *supra* note 8, at 44158 (to be codified at 12 C.F.R. § 331.4(e)).

rule is intended to “closely align[]” with the OCC’s rule “to maintain parity between State banks and national banks with respect to interest rate authority.”¹¹

The OCC and FDIC rules also clarify that the interest charged on a loan that is permissible when the loan is made remains valid despite any subsequent sale, assignment, or other transfer of the loan (or, in the case of the FDIC rule, a change in state law). The OCC emphasized that its rule was “inform[ed]” by the valid-when-made doctrine that has been well established in federal common law for over a century.¹² The FDIC, by contrast, took the position that the permissibility of interest must be determined when the loan is made, not because of the common law valid-when-made doctrine, but because such a rule protects the parties’ expectations and reliance interests and promotes the safety and soundness of banks seeking to generate liquidity or reduce concentrations by selling loans.¹³

The new rules are significant because they bring the agencies’ interpretive expertise to bear on an issue that has been in flux since *Madden*. The significance of the rules, however, will depend on how much deference courts are willing to give to the agencies’ interpretation.¹⁴ The attorneys general of several states filed a lawsuit against the OCC and the FDIC in July and August 2020, respectively, raising that very issue, arguing that the rules are “beyond the [agencies’] power to issue, [are] contrary to statute, and would facilitate predatory lending.”¹⁵ Nevertheless, the regulations should improve the likelihood that courts will revisit or decline to follow *Madden*, especially given the sharp criticism of *Madden* since the decision was issued.¹⁶

NEW LAWSUITS AND DECISIONS

After the OCC and the FDIC published and finalized their rules, one Colorado federal court issued a decision deferring to the OCC’s *Madden*-fix rule and two New York federal courts carved out an exception to *Madden*’s holding, underscoring the uncertainty created by that decision. Before those rules were finalized, however, one Colorado state trial court issued a decision expressly adopting *Madden*.

11. *Id.* at 44150.

12. OCC Final *Madden*-Fix Rule, *supra* note 8, at 33532.

13. FDIC Final *Madden*-Fix Rule, *supra* note 8, at 44146, 44151.

14. *See, e.g., Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 747 (1996) (deferring to the OCC’s regulation defining “interest” under the NBA and upholding regulation because it represents a reasonable interpretation).

15. Complaint for Declaratory and Injunctive Relief at para. 1, *People v. OCC*, No. 20-cv-5200 (N.D. Cal. July 29, 2020); Complaint for Declaratory and Injunctive Relief at para. 1, *People v. FDIC*, No. 4:20-cv-05860 (N.D. Cal. Aug. 20, 2020).

16. *See, e.g., U.S. DEP’T OF TREASURY, A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: NON-BANK FINANCIALS, FINTECH, AND INNOVATION* 11 (July 2018) (“Treasury recommends eliminating constraints brought about by recent court cases that would unnecessarily limit the functioning of U.S. credit markets. Congress should codify the ‘valid when made’ doctrine”); Charles M. Horn & Melissa R. H. Hall, *The Curious Case of Madden v. Midland Funding and the Survival of the Valid-When-Made Doctrine*, 21 N.C. BANKING INST. 1, 22 (2017) (noting a “general consensus that *Madden* was wrongly decided”).

A Colorado federal district court in *Rent-Rite Superkegs West, Ltd. v. World Business Lenders, LLC*¹⁷ upheld that portion of a bankruptcy court's decision finding that section 27 of the FDIA permitted a Wisconsin state-chartered bank to charge interest on a loan at rates permissible in Wisconsin, even after the bank had assigned its rights under the loan agreement to a nonbank.¹⁸ The district court first remarked that it was "convinced" by *Madden*, and that it disagreed with the bankruptcy court's assertion that *Madden* was "incorrectly decided."¹⁹ Nevertheless, the district court rejected *Madden* "[i]n accordance with" the OCC's new *Madden*-fix rule, holding that "a promissory note with an interest rate that was valid when made . . . remains valid upon assignment to a non-bank."²⁰ Although it deferred to the OCC's new rule, the district court reversed and remanded the bankruptcy court's decision to allow the parties to conduct discovery on another issue it said was "introduce[d]" by the rule: "whether [the nonbank] was the true lender."²¹

The *Superkegs* case is notable for two reasons. First, the decision marks the first time a court has deferred to either the OCC's or the FDIC's *Madden*-fix rule. Second, the case caught the attention of the FDIC and the OCC: after the borrower appealed the bankruptcy court's decision to the district court, the FDIC and OCC submitted an amicus brief in support of affirmance. In their brief, the agencies declared that "*Madden*'s disregard of two centuries of established law—without even addressing such law—is not just wrong; it is unfathomable."²²

Meanwhile, two New York federal courts took a different approach to *Madden* by carving out an exception to its holding. In both cases, *Petersen v. Chase Card Funding, LLC*²³ and *Cohen v. Capital One Funding, LLC*,²⁴ plaintiffs sought to challenge credit card loans made by a national bank as usurious under New York law.²⁵ After originating the loans, the national banks securitized and sold the receivables generated by the loans to nonbank entities.²⁶ The nonbank entities, the only defendants named in the cases, moved to dismiss the complaints, arguing

17. No. 19-cv-01552-RBJ (D. Colo. Aug. 12, 2020) (order), ECF No. 31.

18. *Id.* at 10.

19. *Id.* at 7–9.

20. *Id.* at 10. Because the case involved FDIA preemption, it is unclear why the court deferred to the OCC's *Madden*-fix rule, as opposed to the FDIC's *Madden*-fix rule, which was final at the time of the district court's decision.

21. *Id.* at 10, 13 (noting that "the rule states that it 'does not address which entity is the true lender'" (citing OCC Final *Madden*-Fix Rule, *supra* note 8, at 33535)).

22. Amicus Brief for the FDIC and OCC in Support of Affirmance and Appellee at 23, *In re Rent-Rite Superkegs W. Ltd. v. World Lenders, LLC*, 603 B.R. 41 (Bankr. D. Colo. 2019) (No. 1:19-cv-01552-REB), 2019 WL 4569774; accord Brief for the United States as Amicus Curiae, *Midland Funding, LLC v. Madden*, 786 F.3d 246 (2d Cir. 2015) (No. 15-610), 2016 WL 2997343, at *6, *12–13 (calling *Madden* "incorrect" and "misconceived").

23. No. 19-CV-00741-LJV-JJM, 2020 WL 5628935 (W.D.N.Y. Sept. 21, 2020).

24. No. 19-CV-3479-KAM-RLM, 2020 WL 5763766 (E.D.N.Y. Sept. 28, 2020).

25. *Petersen*, 2020 WL 5628935, at *1–2; *Cohen*, 2020 WL 5763766, at *1.

26. *Petersen*, 2020 WL 5628935, at *2; *Cohen*, 2020 WL 5763766, at *3.

that the plaintiffs' claims were preempted by the NBA.²⁷ The plaintiffs opposed the motions, relying on *Madden*.²⁸

In granting the motions, the district courts declined to apply *Madden* to the credit card securitization programs at issue.²⁹ Both courts distinguished *Madden* on the ground that the national banks in *Madden* "sold [the loans at issue] outright to a new, unrelated owner, divesting [themselves] completely of any continuing interest in them."³⁰ In the securitization programs at issue in the New York cases, however, the national banks continued to own the accounts, which allowed the banks to modify the accounts' terms and conditions, including the interest rate charged to borrowers.³¹ Therefore, the courts reasoned, *Madden* did not preclude a finding that the plaintiffs' claims were preempted.³²

Although both courts went on to hold that the plaintiffs' claims were preempted, the courts sidestepped the OCC's new *Madden*-fix rule. Instead, the courts examined whether the state law was impliedly preempted under the Supreme Court's *Barnett Bank* preemption framework, under which a state law is preempted if it "prevents or significantly interferes with the exercise by a national bank of its powers."³³ Since "[a]pplying New York's usury limits would significantly interfere with [the national bank's] ability to exercise its power to charge interest on the loans it issues, to sell interests in loan contracts, and to participate in the securitization market," the *Cohen* court held, "the NBA preempts Plaintiffs' state law usury claims."³⁴ Like the court in *Cohen*, the court in *Petersen* did not expressly rely on the OCC's *Madden*-fix for its holding that the state-law claims were preempted, but "defer[red] to the OCC's reasoned judgment that enforcing New York's usury laws against the [nonbank] defendants would significantly interfere with [the national bank's] exercise of its NBA powers."³⁵ In the alternative, the *Petersen* court held that the plaintiff's claims are "expressly preempted" because "a national bank . . . sets the interest rate on [the plaintiff's] account" and, under the NBA, "it may do so at the 'interest . . . rate allowed by the laws of the State . . . where the bank is located.'"³⁶

27. *Petersen*, 2020 WL 5628935, at *1; *Cohen*, 2020 WL 5763766, at *4.

28. *Petersen*, 2020 WL 5628935, at *6; *Cohen*, 2020 WL 5763766, at *4.

29. *Petersen*, 2020 WL 5628935, at *6; *Cohen*, 2020 WL 5763766, at *14. The *Petersen* court adopted a magistrate judge's recommendation to grant the motion to dismiss, which had been issued on January 22, 2020. *Petersen v. Chase Card Funding, LLC*, No. 19-CV-00741-LJV-JJM, 2020 WL 613531 (W.D.N.Y. Jan. 22, 2020), *report & recommendation adopted*, 2020 WL 5628935 (W.D.N.Y. Sept. 21, 2020).

30. *Petersen*, 2020 WL 5628935, at *6 (quoting *Madden*, 786 F.3d at 252 n.2); *Cohen*, 2020 WL 5763766, at *14 (quoting *Madden*, 786 F.3d at 252 n.2).

31. *Petersen*, 2020 WL 5628935, at *6; *Cohen*, 2020 WL 5763766, at *15.

32. See *supra* note 31.

33. *Petersen*, 2020 WL 5628935, at *4 (quoting 12 U.S.C. § 25b(b)(1)(B) (setting forth preemption standard "in accordance with the legal standard for preemption in the decision of the Supreme Court of the United States in *Barnett Bank of Marion Cnty., N.A. v. Nelson*, 517 U.S. 25 (1996)" (alterations omitted)); *Cohen*, 2020 WL 5763766, at *9 (quoting 12 U.S.C. § 25b(b)(1)(B)).

34. *Cohen*, 2020 WL 5763766, at *11.

35. *Petersen*, 2020 WL 5628935, at *7.

36. *Id.* at *6 (quoting 12 U.S.C. § 85).

Before the FDIC and OCC *Madden*-fix rules were both finalized, a Colorado state court reached a different decision in one of two twin suits brought against marketplace lenders Avant of Colorado LLC and Marlette Funding by the administrator of Colorado's Uniform Consumer Credit Code.³⁷ The trial court granted the administrator's motion in *Fulford v. Marlette Funding, LLC*³⁸ for a determination of law that Cross River Bank, which made the loans at issue, "cannot export its interest rate to a nonbank such as Defendant Marlette."³⁹ The court agreed with the administrator that its claims were not preempted under section 27 of the FDIA because Cross River Bank "can assign loans to other banks with interest rates greater than those allowed by Colorado, or discount the loans if assigned to non-banks," and therefore "Colorado law[] does not prevent or significantly interfere with the bank's exercise of its powers"—adopting the same reasoning as *Madden*.⁴⁰ As of August 2020, the court had not ruled on a similar motion filed in *Avant*.

With respect to the FDIC and OCC's *Madden*-fix rules, the court "accept[ed] that these federal agencies are entitled to some deference," but nevertheless declined to extend any deference because "the rule proposals [were] not yet law" as of the date of the court's decision in June 2020.⁴¹ In August 2020, the parties in *Marlette* and *Avant* entered into a joint settlement covering both cases, under which the banks and marketplace lenders agreed to collectively pay \$1.55 million.⁴²

TRUE LENDER DEVELOPMENTS

NEW FEDERAL REGULATIONS

The OCC's and FDIC's final *Madden*-fix rules expressly did "not address which entity is the true lender when a bank transfers a loan to a third party."⁴³ In October 2020, however, the OCC finalized a rule declaring that a national bank or federal savings association is deemed to have "made" a loan for purposes of applying federal interest-rate preemption if, "as of the date of origination," the

37. See Catherine M. Brennan & Latif Zaman, *True Lender Developments: Litigation and State Regulatory Actions*, 74 *BUS. LAW.* 545, 548–49 (2019) (in the 2019 *Annual Survey*) (reporting on earlier developments in these suits); Catherine M. Brennan et al., *True Lender Developments: Litigation and State Regulatory Actions*, 73 *BUS. LAW.* 535, 539–40 (2018) (in the 2018 *Annual Survey*) (same).

38. No. 17-CV-30376 (Colo. Dist. Ct. filed Jan. 27, 2017).

39. See Order Regarding Plaintiff's Motion for Determination of Law at 5–7, *Fulford v. Marlette Funding, LLC*, No. 17-CV-30376 (Colo. Dist. Ct. June 9, 2020) [hereinafter *Marlette Summary Judgment Order*].

40. *Id.* at 9.

41. *Id.* The OCC and FDIC rules became effective in August 2020. OCC Final *Madden*-Fix Rule, *supra* note 8, at 33530; FDIC Final *Madden*-Fix Rule, *supra* note 8, at 44146.

42. The settlement was filed as an exhibit to a stipulation to dismiss. Stipulation to Dismiss, Ex. A, Assurance of Discontinuance at 14–15, *Fulford v. Marlette Funding, LLC*, No. 17-CV-30376 (Colo. Dist. Ct. Aug. 18, 2020) [hereinafter *Avant/Marlette Settlement*].

43. OCC Final *Madden*-Fix Rule, *supra* note 8, at 33534; see also FDIC Final *Madden*-Fix Rule, *supra* note 8, at 44153 ("[T]he rule does not address the question of whether a State bank or insured branch of a foreign bank is a real party in interest with respect to a loan or has an economic interest in the loan under state law, e.g., which entity is the true lender.").

federally chartered institution “[i]s named as the lender in the loan agreement” or “[f]unds the loan.”⁴⁴ If one bank is named as the lender in the loan agreement and another bank funds the loan, the OCC’s rule clarifies that “the bank that is named as the lender in the loan agreement makes the loan.”⁴⁵

The OCC’s bright-line standard attempts to eliminate the uncertainty caused by fact-intensive, multifactor tests that some courts have applied to determine which entity makes a loan.⁴⁶ As the OCC recognized, “[t]his uncertainty may discourage banks from entering into lending partnerships [with third parties], which, in turn, may limit competition, restrict access to affordable credit, and chill the innovation that can result from these relationships.”⁴⁷ Under the new rule, by contrast, the OCC reasoned that stakeholders can “reliably determine the applicability of key laws, including the law governing the permissible interest that may be charged on the loan.”⁴⁸

The OCC acknowledged that some expressed concern that its rule might facilitate inappropriate “rent-a-charter” lending schemes, where a bank allegedly receives a fee to make loans on behalf of a third party, enabling the third party to evade state laws, such as usury caps.⁴⁹ The attorneys general of several states filed a lawsuit against the OCC in January 2021, seeking to invalidate the rule and echoing these same concerns.⁵⁰ The OCC rejected the assertion that its rule will facilitate such schemes, emphasizing that the OCC will hold banks accountable for compliance with the “robust supervisory framework” that applies to any loan made by a bank and to all third-party relationships to which banks are a party.⁵¹ “If a bank fails to satisfy its compliance obligations,” the OCC stated, it “will use all the tools at its disposal, including its enforcement authority.”⁵²

NEW LAWSUITS AND DECISIONS

Bank partnerships often struggle to prevail in “true lender” cases.⁵³ The Colorado suits against Avant and Marlette, discussed above in connection with

44. National Banks and Federal Savings Associations as Lenders, 85 Fed. Reg. 68742, 68747 (Oct. 30, 2020) (to be codified at 12 C.F.R. pt. 7) [hereinafter OCC Final True Lender Rule] (effective Dec. 29, 2020).

45. *Id.*

46. See, e.g., CFPB v. CashCall, Inc., No. CV 15-7522-JFW (RAOx), 2016 WL 4820635, at *6 (C.D. Cal. Aug. 31, 2016) (examining “which party or entity has the predominant economic interest in the transaction,” including by evaluating how long the entity named as the lender held the loan before selling it to the third party and whether the third party advanced money that the named lender drew upon to make the loans); CashCall, Inc. v. Morrissey, No. 12-1274, 2014 WL 2404300, at *7 (W. Va. May 30, 2014) (noting that the lower court evaluated whether the third party agreed to indemnify the named lender and how the third party treated the loans for financial reporting purposes).

47. OCC Final True Lender Rule, *supra* note 44, at 68742.

48. *Id.* at 68742.

49. *Id.* at 68745.

50. Complaint at para. 130, People v. OCC, No. 1:21-cv-00057 (S.D.N.Y. Jan. 5, 2021) (alleging that the rule will “facilitate rent-a-bank schemes”).

51. *Id.* OCC Final True Lender Rule, *supra* note 44, at 68745.

52. *Id.*

53. See, e.g., Commonwealth v. Think Fin., Inc., No. 14-cv-7139, 2016 WL 183289, at *1, *13 (E.D. Pa. Jan. 14, 2016) (denying motion to dismiss on federal preemption grounds where a plaintiff

valid-when-made litigation, illustrate the challenges these partnerships can face and that the OCC's true lender rule is designed to address. In those cases, the Colorado UCCC administrator separately moved for summary judgment on the grounds that the true lenders on the consumer loans were the nonbank fintech companies, not the banks.⁵⁴ The administrator pointed to a number of factors: the nonbanks' obligation to buy all loans within three days; the nonbanks' maintenance of large "security accounts" with the banks; the nonbanks' indemnification of the banks and reimbursement of expenses related to the loan program; and the nonbanks' right to nearly all the income from the loans.⁵⁵ In its order granting the administrator's motion for a determination of law in *Marlette*, the court noted that the question of whether the first transaction was "valid" under the valid-when-made doctrine "is explored further in the Court's Order regarding summary judgment, but suffice it to say, if Marlette were the 'true lender,' then the interest rates associated with the loans in question were invalid in the first instance under Colorado usury law."⁵⁶ However, the parties entered into a settlement in August 2020,⁵⁷ and the court never issued that summary judgment order.

However, one recent case shows that bank partnerships can prevail in some cases. In this case, an arbitrator rejected a borrower's true lender attack and awarded over \$3 million to the bank defendant, Celtic Bank.⁵⁸ The plaintiff, retailer NRO Boston, had brought claims in 2018 based on the argument that Celtic Bank's partner fintech company, Kabbage, Inc., was the true lender on business loans made by Celtic Bank to NRO and, therefore, claimed that the usury laws of the borrower's home state, Massachusetts, governed the loans.⁵⁹

The arbitrator found that contrary to plaintiffs' theory, Celtic Bank was indeed the true lender, not Kabbage, based on the financial risk that Celtic Bank incurred and its close involvement in the loan program.⁶⁰ After Celtic Bank's motion to confirm the award was briefed, the parties agreed to a consent judgment affirming the arbitrator's award: \$3.3 million from plaintiffs to Celtic Bank, including unpaid loan amounts, costs, and attorneys' fees.⁶¹

alleged that a nonbank "was the de facto lender—marketing, funding and collecting the loan"); *Ubaldi v. SLM Corp.*, 852 F. Supp. 2d 1190, 1203 (N.D. Cal. 2012) (denying motion to dismiss on federal preemption grounds where a plaintiff alleged that a nonbank was the "de facto lender").

54. See, e.g., Plaintiff's Motion for Partial Summary Judgment Regarding the True Lender of the Best Egg Loans at 18–19, *Fulford v. Marlette Funding, LLC*, No. 17-CV-30376 (Colo. Dist. Ct. Jan. 13, 2020).

55. *Id.* at 19–23.

56. *Marlette Summary Judgment Order*, *supra* note 39, at 9.

57. *Avant/Marlette Settlement*, *supra* note 42, at 1.

58. The arbitrator's opinion was filed in the proceeding to confirm the arbitration award. See Declaration of Eric Petersen in Support of Celtic Bank's Motion for Confirmation of Arbitration Award, Ex. 1, Final Award, *NRO Boston, LLC v. Kabbage, Inc.*, No. 1:17-cv-11976 (D. Mass. Sept. 9, 2019) [hereinafter *NRO Final Award*]. Covington & Burling LLP, whose lawyers authored this survey, represented Celtic Bank in this matter.

59. See Brennan & Zaman, *supra* note 37, at 545–47.

60. *NRO Final Award*, *supra* note 58, at 10–11.

61. See *NRO Final Award*, *supra* note 58, at 21 (specifying award amounts); Consent Judgment at paras. 2, 4, *NRO Boston, LLC v. Kabbage, Inc.*, No. 1:17-cv-11976 (D. Mass. May 1, 2020) (confirming arbitrator's award and awarding \$3,299,621.97 to defendant Celtic Bank).

One other new and noteworthy true lender action has also been filed. In *District of Columbia v. Elevate Credit, Inc.*,⁶² the attorney general for the District of Columbia claimed that the nonbank Elevate was the true lender on loans made through two personal loan programs that it operates in partnership with Utah-chartered FinWise Bank and Kentucky-chartered Republic Bank & Trust Company.⁶³ Regarding one of the two loan programs, the complaint alleges that Elevate funds the loans through a “captive credit financing relationship” with a specific third party.⁶⁴ In both loan programs, after the loans are made, special purpose vehicles that are allegedly controlled by Elevate buy a 90 or 96 percent interest in the loan receivables.⁶⁵ The attorney general asserted claims for usury and violations of the District’s consumer protection statutes and requested damages and restitution for consumers, civil penalties, and injunctive and declaratory relief.⁶⁶

THREE TRIBAL LENDER CASES

Three cases involving partnerships between nonbanks and “tribal lenders,” entities affiliated with Native American tribes that are not bound by state usury laws due to the tribes’ sovereign immunity, dealt with similar true-lender arguments as partnerships between banks and nonbanks. The first of these cases, *Williams v. Big Picture Loans, LLC*,⁶⁷ marks the first time that a federal court of appeals has upheld a tribal lending arrangement involving third parties.⁶⁸ The tribe’s lending entity originally contracted with a non-tribal company to perform loan-related services, but it soon changed the structure of its operations after a state regulator sent the lending entity a cease-and-desist letter claiming that it was violating New York’s usury law.⁶⁹ The district court held that the two tribal entities formed as part of the restructuring were not protected by the tribe’s sovereign immunity because the “driving force” behind their formation was “to shelter outsiders from the consequences of their otherwise illegal actions.”⁷⁰ But the Fourth Circuit reversed, observing that the entities had also allowed the tribe to continue its lending operations and therefore were not intended “solely, or even primarily, to protect and enrich a non-tribe member.”⁷¹

The second case, *Solomon v. American Web Loan*,⁷² was a consumer class action filed in late 2017 regarding a complex arrangement between defendant Mark

62. No. 2020-CA-002697-B (D.C. Super. Ct. filed June 5, 2020).

63. Complaint for Violations of the Consumer Protection Procedures Act at paras. 1–3, 10, *District of Columbia v. Elevate Credit, Inc.*, No. 2020-CA-002697-B (D.C. Super. Ct. June 5, 2020).

64. *See id.* at para. 38.

65. *See id.* at paras. 41–43, 73–75.

66. *See id.* at paras. 80–103. Elevate removed the case to federal court on July 2, 2020, where it remains pending. Notice of Removal, *District of Columbia v. Elevate Credit, Inc.*, No. 1:20-cv-01809 (D.D.C. July 2, 2020).

67. 929 F.3d 170 (4th Cir. 2019).

68. *Id.* at 185.

69. *Id.* at 174–75.

70. *Id.* at 175–76.

71. *Id.* at 179.

72. 375 F. Supp. 3d 638 (E.D. Va. 2019).

Curry and a variety of corporate and tribal entities.⁷³ In 2019, a Virginia federal district court held that the lending arrangement was not protected by tribal sovereign immunity, largely because Curry, not the tribe, received most of the revenue from the loan program and “exercise[d] virtually total control” over the lending entity; the tribe could not make any changes without at least one Curry-controlled vote on the board.⁷⁴ In the face of these rulings, the parties reached a preliminary class settlement on the following terms: \$65 million cash, \$76 million in loan cancellation, Curry’s resignation, and other non-monetary relief.⁷⁵

Finally, true lender issues also arose in a criminal case, *United States v. Grote*.⁷⁶ In *Grote*, the defendants operated a series of payday loan programs, including a number of partnerships with tribal lenders. Although the tribes’ involvement was wholly nominal, the defendants went to extreme lengths to create the impression that the tribes owned and controlled the loans. For example, they instructed their phone operators to pretend that they were located on reservations rather than in the defendants’ offices.⁷⁷ After a five-week trial, a jury convicted the defendants of fourteen charges, including wire fraud, money laundering, and collection of unlawful debt. The Second Circuit affirmed the convictions in June 2020.⁷⁸

CONCLUSION

Partnerships between banks and nonbanks serve an important function, especially as financial services move increasingly to online and mobile lending. The regulatory resolution of *Madden* and “true lender” issues, which provides clarity and certainty around lawful partnerships, serves the interests of banks, nonbank lenders, consumers, and small business borrowers, while other means exist to curb the unlawful use of partnership structures.⁷⁹

73. See *id.* at 646, 648–51.

74. See *id.* at 654–61.

75. See *Solomon v. Am. Web Loan*, No. 4:17cv145, 2020 WL 3490606, at *1 (E.D. Va. June 26, 2020).

76. 961 F.3d 105, 112 (2d Cir. 2020).

77. See *id.* at 112.

78. See *id.* at 108–09.

79. See, e.g., *Examination Guidance for Third-Party Lending*, FED. DEPOSIT INS. CORP. 1, 13 (July 29, 2016), <https://www.fdic.gov/news/financial-institution-letters/2016/fil16050a.pdf> (explaining that lending relationships between banks and third parties may provide banks with the ability to “supplement, enhance, or expedite lending services for their customers” and “lower costs of delivering credit products,” and that “enforcement actions may instruct institutions to discontinue third party lending” if serious deficiencies exist in the relationship); *Guidance for Managing Third-Party Risk*, FED. DEPOSIT INS. CORP. (June 6, 2008), <https://www.fdic.gov/news/financial-institution-letters/2008/fil08044a.html> (explaining that “[a]ppropriate corrective actions, including enforcement actions, may be pursued for deficiencies related to a third-party relationship”); *Third-Party Relationships: Risk Management Guidance*, OCC (Oct. 30, 2013), <https://www.occ.gov/news-issuances/bulletins/2013/bulletin-2013-29.html> (explaining that the OCC “will pursue appropriate corrective measures, including enforcement actions, to address violations of law and regulations or unsafe and unsound banking practices by the bank or its third party”).